HMRC - CFM56030 - Unallowable Purposes: Allowance Of Accumulated Net Losses

Allowance of accumulated net losses

The unallowable purpose rule at S690 is most likely to apply in cases where the contract will always produce debits, and the only credits would be exchange gains. However, there may be cases where credits will arise either in the same period (for example, in an interest-rate swap where LIBOR is swapped for say 0.5% fixed) or in different periods. In this respect derivative transactions differ from loan relationships, so there are special rules at CTA09/S692 to recognise this. The result of these special rules is to ring-fence the unallowable ‘tainted’ debits so that they may be set only against credits from the same contract but not against any other profits.

Under S692 it is the ‘amount of the excess accumulated net losses’ of a contract for an accounting period that is brought into account as a debit for that period.

The ‘amount of the excess accumulated net losses’ is found as follows:

Step 1: Add together the amount of any net loss arising for the accounting period and earlier accounting periods. The amount of a ‘net loss’ is the excess of unallowable debits falling within S690(3) over disregarded exchange credits falling within S690(2) in respect of the contract.

Step 2: Deduct from the result of Step 1 any amount which was brought into account under this section (S692) in any earlier accounting period.

Step 3: Add together the amount of any credits (other than exchange credits) arising in respect of the contract for the accounting period or any earlier accounting period.

Step 4: Deduct from the result of Step 3 (but not so as to reduce it below nil) so much of any debits arising in respect of the contract for the accounting period or any earlier accounting period that is not excluded by S690(3) as being referable to an unallowable purpose, and any amount which was brought into account in accordance with this section (S692) in any earlier accounting period.

Step 5: Compare the result of Step 2 and Step 4. The ‘amount of the excess accumulated net loss’ for the period is the lower of these two results.

The effect of these rules is that

exchange credits referable to an unallowable purpose are not brought into account, but

the amount of other credits taxed in an earlier accounting period is available to reduce the amount of any S690 disallowance in respect of debits arising on the same derivative contract in a later accounting period.

See examples at CFM56040.

Previous page

Next page